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In the Supreme Court of the United States

OCTOBER TERM, 1955

No. ——

FRANCIS R. SMITH, COLLECTOR OF INTERNAL REVENUE, PETITIONER

v.

THE CURTIS PUBLISHING COMPANY

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

The Solicitor General, on behalf of Francis R. Smith, Collector of Internal Revenue, prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Third Circuit.

OPINIONS BELOW

The District Court's findings of fact, discussion, and conclusions of law (R. 24a-35a; Appendix A, *infra*, pp. 12-24) are reported at 124 F. Supp. 508. The *per curiam* opinion of the Court of Appeals (Appendix A, *infra*, pp. 25-26) is reported at 220 F. 2d 748.

JURISDICTION

The judgment of the Court of Appeals (Appendix A, *infra*, pp. 26-27) was entered on April 25, 1955. The jurisdiction of this Court is invoked under 28 U.S.C., Section 1254 (1).

QUESTION PRESENTED

In 1947 and 1948 the taxpayer borrowed an aggregate amount of $7,200,000, in three separate borrowings, from nine separate commercial banking institutions and trust companies pursuant to a single loan agreement which provided for repayment over a period of four years, imposed extensive conditions and limitations on the borrower, and granted other privileges and benefits to the lenders for the protection of their investments. The question presented is whether the instruments evidencing these loans are subject to the documentary stamp tax imposed by Sections 1800 and 1801 of the Internal Revenue Code of 1939 on "all bonds, debentures, or certificates of indebtedness issued by any corporation".

STATUTE AND REGULATIONS INVOLVED

Internal Revenue Code of 1939:

SEC. 1800. IMPOSITION OF TAX.

There shall be levied, collected, and paid, for and in respect of the several bonds, debentures, or certificates of stock and of indebtedness, and other documents, instruments, matters, and things mentioned and described in sections 1801 to 1807, inclusive, or for or in respect of the

vellum, parchment, or paper upon which such instruments, matters, or things, or any of them, are written or printed, the several taxes specified in such sections.

(26 U.S.C. 1952 ed., Sec. 1800.)

SEC. 1801. [As amended by Section 1 of the Revenue Act of 1939, c. 247, 53 Stat. 862; Section 209 of the Revenue Act of 1940, c. 419, 54 Stat. 516; and Section 521(a)(3) of the Revenue Act of 1941, c. 412, 55 Stat. 687]. CORPORATE SECURITIES.

On all bonds, debentures, or certificates of indebtedness issued by any corporation, and all instruments, however termed, issued by any corporation with interest coupons or in registered form, known generally as corporate securities, on each $100 of face value or fraction thereof, 11 cents: * * *.

(26 U.S.C. 1952 ed., SEC. 1801.)

Treasury Regulations 71 (1941 ed.), promulgated under the Internal Revenue Code of 1939:

SEC. 113.50. *Scope of Tax.*—Section 1801 imposes a tax upon the issue by any corporation of bonds, debentures, certificates of indebtedness, and all instruments, however termed, with interest coupons or in registered form and known generally as corporate securities. Every renewal of the above described instruments is taxable as a new issue.

* * * * *

SEC. 113.55. *Issues Subject to Tax.* Ordinarily, a corporate instrument styled a bond, debenture or certificate of indebtedness is subject to the tax. However, the taxability of an instrument is not determined by the name alone but depends upon all the circumstances, such as the name, form, and terms of the instrument, etc. Hence, an instrument, however designated, having all the essential characteristics of a bond, debentures, or certificate of indebtedness is taxable as such. Similarly, an instrument issued with interest coupons, or with provision for registration, and coming within the class known generally as corporate securities will be held subject to the tax regardless of the name by which it may be called.

STATEMENT

The facts found by the District Court (R. 24a-32a,), based on a stipulation of the parties (R. 2a-6a), documentary evidence (R. 7a-23a), and oral testimony (R. 1b-17b), may be summarized as follows:

The Curtis Publishing Company, herein referred to as the taxpayer, is a Pennsylvania corporation with its principal place of business in Philadelphia. On June 13, 1947, the taxpayer, pursuant to a previous authorization by its board of directors (R. 7a-8a), entered into a loan agreement with nine separate commercial banks and trust companies located in the New York and Philadelphia area under which the banks agreed to lend to the tax-

payer at any time and from time to time until December 31, 1948, sums in specified proportions, ranging from $150,000 to $1,000,000, but not to exceed an aggregate of $7,200,000 at any one time. The loan agreement (R. 10a-22a) provided that each borrowing should be in the amount of $180,000 or multiples thereof, evidenced by notes in a form agreed to (R. 9a, 13a), and was to be prorated among the several lending banks on the basis of their several commitments under the agreement. (R. 2a-3a, 24a-26a.)

The principal amount of each note was to be repaid in consecutive quarterly installments beginning March 31, 1949, at the rate of 5/72 of the principal for each installment during the calendar years 1949 and 1950, and at the rate of 4/72 of the principal for each installment during the calendar years 1951 and 1952, each note to bear interest at the rate of 2⅛% per annum on the unpaid balance, payable quarterly. (R. 3a-4a, 26a) The loan agreement (R. 10a-22a) also contained extensive and detailed provisions, conditions, and limitations on the activities of the borrower for the protection of the lenders commonly found in this type of agreement, including provisions for repayment.

More particularly, under the loan agreement the taxpayer made certain representations concerning its financial position as of June 13, 1947, the date of the agreement. These representations included warranties that the taxpayer's financial condition was as shown in previously issued financial statements; that no litigation was pending which would

adversely affect its financial position; that the notes to be issued pursuant to the agreement were issuable within the taxpayer's corporate powers and would be enforceable obligations; that it and its subsidiaries were duly organized and chartered; and that all municipal liens on the property of the taxpayer and its subsidiaries had either been discharged or were being contested in good faith. (R. 11a-12a.)

In addition, the taxpayer covenanted that until all loans made under the agreement were repaid it would (1) keep and cause its subsidiaries to keep their corporate franchises in full force and effect and comply with all applicable laws; (2) furnish financial statements periodically and such other additional information as the banks might request; (3) keep its own and its subsidiaries' properties adequately insured; (4) pay when due all taxes assessed against it or its subsidiaries, except those contested in good faith; (5) maintain the consolidated net working capital of the taxpayer and certain subsidiaries at not less than $9,000,000; and (6) maintain a ratio of current assets to current liabilities of not less than one and one-half to one for itself and certain subsidiaries. (R. 15a-17a.)

The taxpayer further covenanted that until all notes were repaid, it and its subsidiaries would not, without the consent of the banks, (1) borrow monies except under the loan agreement; (2) mortgage their properties except under specified circumstances; (3) redeem, purchase, or otherwise acquire for value any of their capital stock except certain

preferred covered by employee agreements; (4) merge, consolidate, or dispose of all or substantially all of their properties; or (5) loan money to or invest in any other business, with certain stated exceptions. (R. 17a-19a.)

Upon default of the taxpayer in any material respect in the observance or performance of the warranties and covenants of the loan agreement, or in the payment of principal or interest, or in the case of insolvency, bankruptcy, receivership, or assignment for the benefit of creditors, the unpaid balance of the notes immediately became due and payable. (R. 19a-20a.)

Pursuant to the above loan agreement the taxpayer made three borrowings: one for $1,800,000 on August 15, 1947, one for $1,800,000 on October 15, 1948, and one for $3,600,000 on December 15, 1948. Each loan was prorated among the nine contracting banks on the basis of their respective commitments. On the dates of the several borrowings the taxpayer delivered to each lending bank a note in the form prescribed by the loan agreement (R. 4a-5a, 9a, 23a-24a) for the amount borrowed from such bank. The notes were identical except for the name of the payee, the date, the face amount, the initial interest payment date, and the amount of the payment installments. They were typewritten on ordinary letter size paper and were signed either by the president or the treasurer of the taxpayer, but did not bear the taxpayer's corporate seal. They were effective on their execution and delivery without further signa-

ture, authentication, or other formality. (R. 4a-5a.) They were in the form of ordinary promissory notes, and, after listing the amount of each installment and its maturity date, provided (R. 23a, 28a-29a):

> This note is one of the Notes described in and is issued pursuant to the terms and conditions of a certain Agreement dated as of June 13, 1947, between the undersigned and certain Banks and Trust Companies to which Agreement reference is hereby made for the rights and obligations affecting the parties.

The loans made to the taxpayer by the nine lending banks were in each instance handled by the bank's commercial loan department, not by its investment department. All installments of principal and interest were paid regularly at maturity by the taxpayer up to and including the quarterly installment due September 30, 1950. On October 3, 1950, the taxpayer prepaid the entire balance of the loans, without premium, from its own funds, and all notes were cancelled on October 4, 1950. (R. 5a-6a, 29a-30a.)

The Commissioner of Internal Revenue assessed documentary stamp taxes pursuant to Sections 1800 and 1801 of the Internal Revenue Code of 1939 in the aggregate amount of $7,920 with respect to the issuance by the taxpayer of the above notes. After payment of the tax the taxpayer duly filed claims for refund of the amounts paid, which were rejected by the Commissioner, and the taxpayer

brought this action to recover. (R. 6a, 30a-31a.) The District Court gave judgment for the taxpayer (R. 36a), and the Court of Appeals affirmed (Appendix A, *infra*, pp. 24-27.)

REASONS FOR GRANTING THE WRIT

This case involves the same issue as that involved in *United States* v. *Leslie Salt Co.*, No. 74, this Term, in which this Court granted a writ of certiorari to the Court of Appeals for the Ninth Circuit on June 6, 1955. A writ should be granted in the instant case for the same reasons which this Court considered sufficient to warrant review in the *Leslie Salt Co.* case.

As in *Leslie Salt Co.*, the stamp tax here in issue is imposed by Sections 1800 and 1801 of the Internal Revenue Code of 1939 (*supra*, pp. 2-3) upon "all bonds, debentures, or certificates of indebtedness issued by any corporation". Our petition for a writ of certiorari filed in that case demonstrates the confusion and contrariety of result obtaining among the lower courts in the effort to define the nature of the instruments falling within the quoted statutory language.

In the instant case the District Court held that the instruments in question were promissory notes and not subject to tax under Sections 1800 and 1801 of the 1939 Code. (R. 32a-35a.) The Court of Appeals affirmed *per curiam* on the authority of the majority opinion in *Niles-Bement-Pond Co.* v. *Fitzpatrick*, 213 F. 2d 305 (C.A. 2d) reprinted as Appendix B, *infra*, pp. 29-49. The majority

opinion of the Second Circuit in the latter case, with Judge Clark dissenting, followed the reasoning of the Seventh Circuit in *Belden Mfg. Co.* v. *Jarecki,* 192 F. 2d 211, and of the Eighth Circuit in *United States* v. *Ely & Walker Dry Goods Co.,* 201 F. 2d 584, and distinguished its own earlier decision in *General Motors Acceptance Corp.* v. *Higgins,* 161 F. 2d 593, certiorari denied, 332 U.S. 810, primarily on the ground that the instruments involved in the *Niles-Bement-Pond* case evidenced loans negotiated with the taxpayer's regular commerical banking institution rather than with investment institutions as in the *General Motors Acceptance Corp.* case.

As indicated in the petition for a writ of certiorari in the *Leslie Salt Co.* case, prior to the decision of the Ninth Circuit in that case, this distinction between instruments evidencing loans negotiated with commercial banking institutions and those evidencing loans negotiated with investment institutions had gained rather wide acceptance in the lower federal courts. However, it has always been the contention of the Government, approved by Judge Clark dissenting in the *Niles-Bement-Pond Co.* case, that the character of the lending institution is not determinative of the taxability of instruments evidencing long-term capital loans of the character involved in these cases. Accordingly, the fact that the loan here was made by a group of commercial banking institutions while the loan in *Leslie Salt Co.* was made by two insurance companies is in our view immaterial. We believe that

the stamp tax was properly imposed in both cases.

The amount of litigation involving this issue and its importance to the revenue are demonstrated in the petition for a writ of certiorari in the *Leslie Salt Co.* case. Since the instant case involves long-term capital loans negotiated with commercial banks rather than with insurance companies and similar investment institutions, certiorari should be granted in order to provide a basis for full exploration and clarification of this widespread problem.

CONCLUSION

It is respectfully submitted that this petition for a writ of certiorari should be granted.

SIMON E. SOBELOFF,
Solicitor General,
H. BRIAN HOLLAND,
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ELLIS N. SLACK,
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JULY 1955.

APPENDIX 'A'

IN THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF PENNSYLVANIA

Civil Action No. 13422

THE CURTIS PUBLISHING COMPANY, PLAINTIFF

v.

FRANCIS R. SMITH, COLLECTOR OF INTERNAL REVENUE, DEFENDANT

SUR PLEADINGS AND PROOF

September 24, 1954.

CLARY, J.

This is an action for the refund of documentary stamp taxes assessed by the Commissioner of Internal Revenue and paid by the taxpayer under Section 1800 of the Internal Revenue Code, 26 U. S. C. § 1800. The Commissioner assessed the taxes upon the plaintiff corporation contending that certain promissory notes issued by that corporation were debentures of such a character as to bring them within the reach of Section 1801 of the Internal Revenue Code, 26 U. S. C. § 1801. The facts of the case have been substantially stipulated between the parties and there is no dispute as to the further facts adduced. Upon pleadings and proof I make the following:

FINDINGS OF FACT

1. Plaintiff is and at all relevant times has been a corporation organized and existing under the

laws of the Commonwealth of Pennsylvania with its registered office and principal place of business in Philadelphia, Pennsylvania. Plaintiff is engaged in the business of publishing magazines. (Stipulation Paragraph 1, R18)

2. Defendant Francis R. Smith was at all relevant times Collector of Internal Revenue for the First Collection District of Pennsylvania. (Paragraphs 1 and 14 of Complaint and Paragraphs 1 and 10 of Answer)

3. Plaintiff desired to obtain additional funds for use in its business. On May 26, 1947, plaintiff's Board of Directors authorized and approved the execution and delivery of a loan agreemcnt with nine banks and authorized certain officers to borrow on behalf of the Company amounts not exceeding $7,200,000. as and when such funds were needed for the purposes of the business. (Stipulation, Paragraph 2, R18)

4. A Loan Agreement, dated June 13, 1947, was entered into between plaintiff and nine banks, namely: Real Estate Trust Company, The Philadelphia National Bank, Tradesmens National Bank and Trust Company, Central-Penn National Bank of Philadelphia, Fidelity-Philadelphia Trust Company, the Pennsylvania Company for Banking and Trusts, The First National Bank of Philadelphia, all of Philadelphia, Pennsylvania, The First National Bank of the City of New York and Central Hanover Bank and Trust Company, both of New York, New York. (Stipulation, Paragraph 3, R18)

5. Under the Loan Agreement the nine banks agreed to lend plaintiff at any time and from time

to time until December 31, 1948, sums in specified proportions not exceeding at any one time the aggregate principal amount of $7,200,000. The banks' respective commitments were as follows:

Bank	Amount
Central Hanover Bank & Trust Co.	$1,000,000
The First National Bank of the City of N. Y.	1,000,000
The First National Bank of Philadelphia	950,000
The Pennsylvania Company for Banking & Trusts	850,000
Fidelity-Philadelphia Trust Company	850,000
Central Penn National Bank of Philadelphia	850,000
Tradesmens National Bank and Trust Company	800,000
The Philadelphia National Bank	750,000
Real Estate Trust Company	150,000
	$7,200,000

(Stipulation, Paragraph 4, R18)

6. The Loan Agreement provided that each borrowing should be in the amount of $180,000. or multiples thereof and was to be prorated between the lending banks on the basis of their respective commitments. Each borrowing from each bank was to be evidenced by a negotiable note in the form attached to the Loan Agreement and denoted therein as Exhibit A. (Stipulation, Paragraph 5, R18)

7. The principal amount of each note was to be paid in consecutive quarterly installments beginning March 31, 1949, at the rate of 5/72 of the principal for each installment during the calendar years 1949 and 1950, and 4/72 of the principal for each installment during the calendar years 1951 and 1952. Each note was to bear interest at the rate of 2⅛% per annum, payable quarterly at the end of each calendar quarter. (Stipulation, Paragraph 6, R18)

8. The Loan Agreement also included provisions substantially as follows:

(A) In Section II plaintiff made certain representations concerning its financial position as of

June 13, 1947, the date of the Loan Agreement. Provision was made for payment of a commitment fee of ¼ of 1% per annum on the unused portion of the maximum credit provided for by the Loan Agreement for the period during which any portion of the credit was unused. (Section V)

(B) Plaintiff at any time or from time to time could prepay any or all of the notes at par and accrued interest, provided that (1) prepayments made before December 31, 1948, (the end of the commitment period) could be made only on at least three banking days notice and as to each note were required to be in whole, but not in part payment, (2) prepayments made after December 31, 1948 required at least thirty days prior notice, and as to each note could be in whole or in part, but if in part, in the inverse order of installment maturities, and (3) any prepayment with funds borrowed from others was subject to a premium of ¼ of 1% on the amount prepaid from the date of payment to the installment maturity date. (Section III D)

(C) Plaintiff covenanted that until all loans were repaid it would (1) keep and cause its subsidiaries to keep their corporate franchises in full force and effect and comply with all applicable laws, (2) furnish financial statements periodically and such other additional information as the banks might request, (3) keep its and its subsidiaries' properties adequately insured, (4) pay when due all taxes assessed against it or its subsidiaries, except those contested in good faith, (5) maintain the consolidated net working capital of plaintiff and certain subsidiaries at not less than $9,000,000., and (6) maintain a current asset ratio of not less

than one and one-half to one for itself and certain subsidiaries. (Section VII)

(D) Plaintiff also covenanted that until all notes were repaid it and its subsidiaries would not without consent of the banks (1) borrow monies except under the Loan Agreement, (2) mortgage its properties except in specified circumstances, (4) merge, consolidate or dispose of all, or substantially all, of its property, (5) loan money to or invest in any other business, with certain stated exceptions. (Section VIII)

(E) An acceleration clause under which all notes should become due forthwith upon the occurrence of specified events of default. (Section IX) (Stipulation, Exhibit B, R18)

9. Pursuant to the Loan Agreement plaintiff made three borrowings, namely, one for $1,800,000. on August 15, 1947, one for $1,800,000. on October 15, 1948, and one for $3,600,000. on December 15, 1948, each borrowing being prorated among the nine banks in accordance with their respective commitments. The proportionate amounts of each borrowing loaned by the respective banks were as follows:

Bank	August 15, 1947 October 15, 1948	December 15, 1948
Central Hanover Bank & Trust Co.	$ 250,000	$ 500,000
The First National Bank of the City of N. Y.	250,000	500,000
The First National Bank of Philadelphia	237,500	475,000
The Pennsylvania Company for Banking & Trusts	212,500	425,000
Fidelity-Philadelphia Trust Company	212,500	425,000
Central-Penn National Bank of Philadelphia	212,500	425,000
Tradesmens National Bank & Trust Company	200,000	400,000
The Philadelphia National Bank	187,500	375,000
Real Estate Trust Company	37,500	75,000
	$1,800,000	$3,600,000

(Stipulation, Paragraph 7, R18)

10. On the dates of the several borrowings, plaintiff delivered to each lending bank a note in the form prescribed by the Loan Agreement for the amount borrowed from such bank. The notes were identical except for the name of the promisee, the date, the face amount, the initial interest payment date and the amounts of the repayment installments. The notes were typewritten on ordinary letter size paper and were signed by either the President or the Treasurer, but did not bear plaintiff's corporate seal. They were effective on their execution and delivery without further signature, authentication or other formality. (Stipulation, Paragraph 8, R18)

The notes were in the form of ordinary promissory notes and after listing each installment and its maturity date provided:

> "This note is one of the Notes described in and is issued pursuant to the terms and conditions of a certain Agreement dated as of June 13, 1947 between the undersigned and certain Banks and Trust Companies to which Agreement reference is hereby made for the rights and obligations affecting the parties."

(Stipulation, Exhibit C, R18)

11. All installments of principal were paid regularly at maturity up to and including the quarterly installment due September 30, 1950, and on October 3, 1950, plaintiff prepaid the entire balances of the loans. Such prepayment was made without premium and from plaintiff's own funds. All interest payments were made as they became due and interest was paid for the period ending

October 3, 1950, when the balances of the loans were paid off. All notes were cancelled October 4, 1950 and returned to plaintiff on October 6, 1950. (Stipulation paragraph 9, R18)

12. Plaintiff had utilized each of the lending banks, with the exception of Fidelity-Philadelphia Trust Company (which became Trustee under plaintiff's Pension Plan in 1945) and Central-Penn National Bank of Philadelphia, at the times the Loan Agreement and loans thereunder were made, and for many years prior thereto as shown by the following table:

Bank	Commencement Date
Central Hanover Bank & Trust Co.	November, 1935
The First National Bank of the City of New York	August, 1939
The First National Bank of Philadelphia	prior to 1923
The Pennsylvania Company for Banking and Trusts	prior to 1923
Fidelity-Philadelphia Trust Company	....
Central-Penn National Bank of Philadelphia	....
Tradesmens National Bank & Trust Co.	January, 1930
The Philadelphia National Bank	prior to 1929
Real Estate Trust Company	prior to 1923

(Stipulation, Paragraph 10, R18)

13. The loans made to plaintiff pursuant to the Loan Agreement by the nine lending banks were in each case handled by the commercial loan department and officers in the regular course of the bank's commercial banking business and not by its investment department. In each case the procedures followed in handling the loans were the same as those observed generally by the bank with respect to commercial loans and the loans were carried in the bank's loan portfolio. (Stipulation, Paragraph 11, R18)

14. No documentary stamp tax was paid upon execution and delivery of any notes, but after examinations and reports by Internal Revenue

Agents documentary stamp taxes were assessed thereon. The assessment on the first two borrowings was $3,960. and this amount was paid by plaintiff to defendant on November 23, 1949, in payment of that assessment. The assessment on the third borrowing was $3,960. and this amount was paid by plaintiff to defendant on August 23, 1950, in payment of that assessment. On December 2, 1949, plaintiff filed a claim for refund of the tax first paid, and the claim for refund was rejected in full on March 23, 1950. On August 17, 1950, plaintiff filed a similar claim for refund of the tax paid in respect of the third borrowing and this was rejected in full on February 14, 1951. (Stipulation, Paragraph 12, R18)

15. Plaintiff filed suit under the Act of June 25, 1948, C. 646, 62 Stat. 932 (Title 28 U.S.C. 1340) for the purpose of obtaining repayment of the documentary stamp taxes paid and the suit was brought within two years of the date of rejection of each of plaintiff's refund claims. (Stipulation, Paragraph 13, R18)

16. In commercial banking practice before an unsecured commercial loan is made, the borrower is usually required to meet certain credit requirements designed to protect the lending bank against credit risks. Generally such requirements are not reduced to writing in the case of short term loans, such as 60 or 90 day loans, but they are nevertheless an integral part of the lending transaction. In general, the same requirements must be satisfied when short term loans are renewed, and the bank by reason of the short maturity is in a position to protect itself against deterio-

rating credit by insisting on payment or reduction. (R31, 32, 38, 52)

17. In commercial banking practice, loans with maturities of more than one year are known as term loans. In the case of term loans, the lending bank does not have the flexibility in self-protection available in short term loans. It is the practice of commercial banks to incorporate provisions in the note or lending agreement covering term loans substantially the same credit requirements it would have insisted on in considering the granting of a short term loan or its renewal. (R25, 39)

18. Term loans range from $3,000. to the lending bank's legal limit, which in the case of the Pennsylvania Company for Banking and Trusts is approximately $4,000,000. If loans exceed this amount, other banks participate either directly, as in plaintiff's loan, or through the medium of participation certificates issued by the lending bank. (R25-27)

19. It is not usual banking practice to sell term loan notes and the instruments evidencing such obligations are not prepared in a manner to promote marketability. The notes are held by the bank, however, with a view to hypothecating them with the Federal Reserve Bank if additional reserves are required. Such notes could ordinarily not be held by a bank as investment under applicable Pennsylvania banking laws.

20. Plaintiff's notes and loan agreement were typical of term loan transactions negotiated by the Pennsylvania Company for Banking and Trusts and the provisions of the loan agreement

were substantially the same as those generally used in such term loan agreements.

Discussion

The result to be reached in this case, in view of the absence of controversy as to facts, involves primarily a question of law and on a point often litigated but always, nevertheless, difficult of decision. It involves the proper interpretation of that portion of the language of Section 1801 of the Internal Revenue Code, 26 U.S.C. §1801, which defines, in part, the instruments intended to be taxed thereby. The pertinent language of the statute is as follows:

> "... all bonds, debentures, or certificate of indebtedness issued by any corporation, and all instruments, however termed, issued by any corporation with interest coupons or in registered form, known generally as corporate securities ..."

Pursuant to authority delegated by Congress the Secretary of the Treasury has promulgated a regulation implementing the terms of the statute and attempting to define debentures. Treasury Regulation 71 (1941 edition), Section 113.55 provides, inter alia, that

> "... an instrument, however designated, having all the essential characteristics of a ... debenture ... is taxable as such."

Unfortunately, the wording of the regulation serves only to pose the elements of the problem of definition rather than to solve it.

The Government contends in this action, as it has in other cases more or less factually similar, that the instruments utttered by The Curtis Publishing Company were "debentures" which fall within the sweep of Section 1801. On the contrary, plaintiff in thorough disagreement earnestly contends that they were bona fide "promissory notes" which are not "debentures" and not subject to the stamp tax. The problem, therefore, narrows itself to one of definition of the word "debentures" as Congress has employed it in this Section of the Internal Revenue Code.

It would serve no useful purpose to make an exhaustive comparative analysis of the facts and reasoning of the cases cited by each party to support its respective contentions. The plaintiff relies upon the reasoning and result reached in *Niles-Bement-Pond Co.* v. *Fitzpatrick,* 112 F. Supp. 132, reversed 213 F. 2d, 305 (C.C.A. 2, 1954); *U. S.* v. *Ely & Walker Dry Goods Co.,* 201 F. 2d, 584 (C.C.A. 8, 1953); *Belden Mfg. Co.* v. *Jarecki,* 95 F. Supp. 539, aff'd. 192 F. 2d, 211 (C.C.A. 7, 1951); *Royal Loan Co., et al.,* v. *U. S.,* 154 F. 2d 556 (C.C.A. 8, 1946), and other cases. Just as strongly to the contrary, the Government contends that *General Motors Acceptance Corporation* v. *Higgins,* 60 F. Supp. 979, reversed 161 F. 2d, 593 (C.C.A. 2, 1947); *Commercial Credit Co.* v. *Hofferbert,* 93 F. Supp. 562, aff'd. per cur. 188 F. 2d 574 (C.C.A. 4, 1951), and other cases correctly apply the statute and must control the result here. The Court of Appeals for the Second Circuit has thoroughly considered the problems arising from use of the word "debentures" in Section 1801 of the Internal Revenue Code in the

GMAC and *Niles-Bement-Pond* decisions. In the *GMAC* case the court held that the documents there involved were debentures and subject to tax. In the *Niles-Bement-Pond* case the court held the instruments to be promissory notes and not subject to tax.

The Niles-Bement Pond and the Curtis loans fairly represent what is apparently an increasingly common corporate credit device. It is, of course, of the utmost importance to both the Treasury Department and the taxpayer that the tax consequences of such a transaction be reasonably predictable. In my opinion the Second Circuit has laid down in a difficult aspect of tax law a workable and legally proper standard which is worthy of preservation and respect. It is the Government's contention that credit instruments such as are here involved were intended to be taxed by Congress, but I cannot discover such intention in the wording of the statute and regulations. The facts in this case indicate a straightforward commercial loan rather than a debenture issue as that term is commonly understood in banking circles. Congress has before at various times in the history of our nation imposed stamp taxes on instruments of the type here involved. However, the last such enactment was repealed in 1924 and has never been reenacted in any form. It would appear, therefore, that had the Congress intended to subject ordinary promissory notes to stamp taxes, it would have used the clearer and more precise terminology of the earlier statutes.

My view of the instant fact situation is that for the purpose of decision the case is identical with the *Niles-Bement-Pond* case. In only two respects

do the facts differ. The term of the Niles-Bement-Pond loan was longer than that granted to this plaintiff, seven years as against something over three years. The amount of the Curtis loan was the larger of the two—$7,200,000. as against $3,125,000. I do not think that either factual situation is of sufficient significance to require a different result. I adopt the reasoning and the result reached in the opinion of Circuit Judge Harlan in the *Niles-Bement-Pond* case.

Conclusions of Law

1. The Court has jurisdiction over the parties to the action and the subject matter thereof.

2. The twenty-seven instruments delivered by plaintiff to the nine lending banks, on which stamp taxes were assessed and paid, were promissory notes and were not debentures or other type of instrument within the meaning of, and subject to tax under, Section 1801 of the Internal Revenue Code.

3. Stamp taxes on said twenty-seven instruments were illegally assessed and collected by defendant Collector of Internal Revenue.

4. Plaintiff is entitled to judgment against defendant in the sum of $7,920.00 together with interest and costs as prescribed by law.

[Caption omitted]

Order

And now, to wit this 24th day of September, 1954, for the reasons set forth in the Findings of Fact and Conclusions of Law filed concurrently herewith, it is

ORDERED, ADJUDGED AND DECREED

that judgment be entered for the plaintiff and against the defendant in the sum of $7,920.00, with interest on $3,960.00 from November 23, 1949 and on $3,960.00 from August 23, 1950, pursuant to the applicable provisions of Section 3771 of the Internal Revenue Code. (26 U.S.C. Sec. 3771).

By the court:

(S.) THOMAS J. CLARY, *J.*

OPINION

UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

No. 11,504

THE CURTIS PUBLISHING COMPANY, A CORPORATION

v.

FRANCIS R. SMITH, COLLECTOR OF INTERNAL REVENUE, APPELLANT

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF PENNSYLVANIA

Argued April 6, 1955

Before, Biggs, *Chief Judge,* and Maris and Hastie, *Circuit Judges*

OPINION OF THE COURT—Filed April 25, 1955

Per CURIAM:

We perceive no error in the decision of the court below. The judgment will be affirmed upon the

reasoning stated in the opinion of Circuit Judge, now Mr. Justice, Harlan in Niles-Bement-Pond Co. v. Fitzpatrick, 213 F. 2d 305 (2 Cir. 1954).

JUDGMENT

UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

No. 11,504

THE CURTIS PUBLISHING COMPANY, A CORPORATION

vs.

FRANCIS R. SMITH, COLLECTOR OF INTERNAL REVENUE, APPELLANT

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF PENNSYLVANIA

Present: Biggs, Chief Judge, and Maris and Hastie, Circuit Judges.

JUDGMENT

This cause came on to be heard on the record from the United States District Court for the Eastern District of Pennsylvania and was argued by counsel

On consideration whereof, it is now here ordered and adjudged by this Court that the judgment of the said District Court in this case be, and the same is hereby affirmed.

Received and Filed April 25, 1955.

APPENDIX 'B'

UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

No. 122. October Term, 1953

Argued March 9, 1954. Decided May 5, 1954

Docket No. 22881

NILES-BEMENT-POND COMPANY, A CORPORATION INCORPORATED UNDER THE LAWS OF THE STATE OF NEW JERSEY AND HAVING ITS PRINCIPAL PLACE OF BUSINESS IN WEST HARTFORD, CONNECTICUT, PLAINTIFF-APPELLANT

v.

JOHN J. FITZPATRICK, COLLECTOR OF INTERNAL REVENUE FOR THE DISTRICT OF CONNECTICUT, DEFENDANT-APPELLEE

Before Clark, Medina and Harlan, Circuit Judges

Appeal from United States District Court for the District of Connecticut, J. Joseph Smith, Judge.

Appeal from a final judgment dismissing on the merits an action for refund of stamp taxes. Reversed.

Benjamin Hinman, Hartford, Conn. (Shipman & Goodwin, Hartford, Conn. of counsel), for plaintiff-appellant.

H. Brian Holland, Assistant Attorney General (Ellis N. Slack, Fred E. Youngman, Special Assistants to the Attorney General, Simon S. Cohen,

United States Attorney, on the brief) for defendant-appellee.

HARLAN, *Circuit Judge:*

This appeal brings before us a question as to the applicability of the stamp tax sections of the Internal Revenue Code, 26 U. S. C. §§ 1800, 1801, to corporate "promissory notes" issued to a banking institution for a loan.

The District Court, after a trial, filed a memorandum decision containing Findings of Fact and Conclusions of Law, and, relying upon our decision in *General Motors Acceptance Corp.* v. *Higgins,* 161 F. 2d 593 (2d Cir.), *cert. denied* 332 U. S. 810 (1947), held that the notes involved should be regarded as corporate debentures and as such subject to stamp taxes under Sections 1800 and 1801.[1] *Niles-Bement-Pond Co.* v. *Fitzpatrick,* 112 F. Supp. 132 (D. Conn. 1953).

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[1] "SECTION 1800. IMPOSITION OF TAX.

There shall be levied, collected, and paid, for and in respect of the several bonds, debentures, or certificates of stock and of indebtedness, and other documents, instruments, matters, and things mentioned and described in sections 1801 to 1807, inclusive, or for or in respect of the vellum, parchment, or paper upon which such instruments, matters, or things, or any of them, are written or printed, the several taxes specified in such sections."

"Section 1801. CORPORATE SECURITIES

On all bonds, debentures, or certificates of indebtedness issued by any corporation, and all instruments, however termed, issued by any corporation with interest coupons or in registered form, known generally as corporate securities, on each $100 of face value or fraction thereof, 11 cents: *Provided,* That every renewal of the foregoing shall be taxed as a new issue * * *."

APPENDIX B

In 1949, Niles-Bement-Pond Company, a manufacturer of machine tools whose principal place of business is at West Hartford, Conn., negotiated a $3,125,000 loan from the National City Bank of New York. The reasons for this loan were to increase the Company's cash and working capital, and to refinance its existing loans, made for like purposes, for longer terms.

The Company issued to the Bank twenty-nine "Promissory Notes," nine in face amount of $125,000 each and 20 each in face amount of $100,000. These notes matured at quarterly intervals over a period of seven years, beginning October 1, 1949 and ending October 1, 1956, with an initial interest rate of 2%, which was stepped up to 2½% beginning with the note maturing January 1, 1952, and to 2¾% beginning with the note maturing July 1, 1954. The notes, all in identical form except as to amounts, maturity dates and interest rates, were each captioned "Promissory Note" and were typewritten-mimeographed on plain white watermarked paper.

These notes were issued under a Loan Agreement pursuant to which Niles-Bement-Pond, among other things, obligated itself to (a) maintain a minimum amount of working capital, (b) keep its properties insured and free from tax and other liens, (c) refrain from incurring any new indebtedness for borrowed money, through the issuance of securities or otherwise, except indebtedness not exceeding $2,000,000 and maturing within one year, (d) refrain from purchase of its own stock, merger or consolidation, or sale of fixed

assets except upon ratable application of any proceeds to the payment of the notes issued to the National City Bank, and (e) submit periodic financial statements to the Bank.

The following additional facts are pertinent: the Loan Department of the National City Bank for many years in the regular course of its business has made loans to the Bank's industrial depositors to meet their temporary working capital requirements and for other purposes. Prior to World War II such loans were initially made on a short term basis, usually varying from 30, 60 or 90 days to six months, and then, if need be, renewed for such further periods as the exigencies of the borrower's business might require.

With the outbreak of World War II many industrial concerns became involved in furnishing supplies to the Government under contracts requiring for their fulfillment the borrowing of larger amounts of temporary working capital and for more extended periods of time. Industrial customers of the Bank engaged in such war work disliked to be faced with continuing maturities inherent in the former practice of 30 days to 6 months borrowings, and also wished to be relieved of the uncertainty as to whether such loans would be renewed or not. To obviate these objections the National City Bank in the early 1940's instituted the practice of making term loans of the type involved here.

Such loans, which are made only to depositors of the Bank, vary in amount from $10,000, in the

case of small businesses, to amounts in excess of the present loan, in the case of larger enterprises. The Bank endeavors to keep the maturities as short as possible, and the longest maturity so far given has been ten years. The interest payable is determined by the current prime rate, with some graduated increase in the case of the longer term loans. The loans are protected by loan agreements restricting to a certain extent the borrower's fiscal activities; and the Bank looks to repayment of the loan from the liquidation of inventories in the normal course of business. The making of such loans is within the province of the Bank's Loan Department, just as are the more usual 30 days to six months loans, in contrast to capital account financing which is handled through the Investment Department of the Bank.

In order to put in focus the issue before us, some reference to the legislative history of stamp taxes on debentures and promissory notes is necessary. From 1898 to 1902 and from 1914 to date, "debentures" as such, among other types of corporate securities, have been subject to stamp taxes at varying rates; and from time to time "promissory notes" have also been subject to stamp taxes, but always in a different paragraph of the taxing Schedules than that fixing the rate of tax on debentures, and always at a lower rate.[2] In 1924

[2] Act of June 13, 1898, 30 Stat. 448, § 6, p. 451, Sch. A, pp. 458-9; Act of March 2, 1901, 31 Stat. 938 (repeal of tax on promissory notes); Act of April 12, 1902, 32 Stat. 96-97 (repeal of all documentary stamp taxes); Act of October 22, 1914, 38 Stat. 745, § 5, p. 753, Sch. A, pp. 759-60 (imposition

the stamp tax on both debentures and promissory notes was repealed, but the tax on debentures and other types of corporate securities, substantially as presently contained in 26 U.S.C., §§1800-1801, was re-enacted. Rev. Act. of 1924, 43 Stat. 253, Tit. XI (Repeals), page 352; Tit. VIII (Stamp Taxes), page 331, Sch. A, page 333. The tax on promissory notes has not been re-enacted since the 1924 repeal.

It thus appears from this taxing history that Congress set apart at least some types of "promissory notes" for different tax treatment than debentures. And if it could be shown that these earlier statutes taxing "promissory notes" embraced the type of promissory note involved in the transaction before us, the final repeal of the "promissory note" tax in 1924 would put the appellant well along the road to a favorable decision in this case.

On the other hand, from a conclusion that the promissory notes here involved are not of the type previously subject to stamp taxes it by no means follows that these notes are nonetheless subject to the debenture tax simply because they

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of tax on bonds, debentures and promissory notes); Act of October 3, 1917, 40 Stat. 300, Tit. VIII, p. 319, Sch. A, Subds. 1, 6, pp. 321-3 (Revenue Act of 1917, carrying forward taxes on bonds, debentures and promissory notes); Act of February 24, 1919, 40 Stat. 1057, Tit. XI, p. 1133, Sch. A, Subds. 1, 6, pp. 1135, 1137 (Revenue Act of 1918 carrying forward same taxes); as amended by Act of November 23, 1921, 42 Stat. 227, Tit. XI, p. 301, Sch. A, Subds. 1, 5, pp. 303, 305 (Revenue Act of 1921, retaining tax on both debentures and promissory notes); Revenue Act of 1924, 43 Stat. 253, Tit. VIII (Stamp Taxes), p. 331, Sch. A, p. 333; I. R. C. §§ 1800, 1801.

are corporate loan instruments. That would depend upon whether the notes, though termed "promissory notes," are in substance debentures within the purview of Section 1801. See *General Motors* case, *supra*. The Treasury itself views the matter in the same light. Treasury Regulation 71, §113.55, relating to Sections 1800 and 1801, provides that "an instrument, however designated, having *all the essential characteristics* of a * * * debenture * * * is taxable as such." (Italics supplied.)

We therefore pass to a consideration of these two aspects of the problem.

The District Court apparently reached the conclusion that the 1924 repealer was intended to reach only the short term promissory notes of individuals. "Thus, Congressional intent seems to have been to relieve the poor *individual* from a burden; it is most probable that the effect of the repeal on corporation paper was given little or no consideration." *Niles-Bement-Pond Co.* v. *Fitzpatrick, supra,* at page 136. But at this point we may observe that the earlier statutes taxing promissory notes did not distinguish between individual and corporate promissory notes nor between notes of different duration, and that the new Revenue Act of 1924 did not preserve stamp taxes on any kind of promissory notes. Nor have we been able to find any indication that Congress thought that the tax on corporate promissory notes as such was preserved by that Section of the 1924 Revenue Act which took over in *haec verba* the section of the earlier statute taxing deben-

tures, among other corporate securities. *Compare* Act of June 2, 1924, 43 Stat. 253, Tit. VIII, Sch. A, Subd. 1, page 333, *with* Act of November 23, 1921, *supra,* at page 303, and Act of February 24, 1919, *supra,* at page 1135.

We may also note Judge Chase's statement in the *General Motors* case, *supra,* that the stamp tax on promissory notes which was repealed in 1924 "was taxation which covered the notes used customarily in day to day commercial transactions of a short term credit character and not instruments, whether called notes or something else, by which a corporation obtained capital for a substantial period of time from investors for general use in its business just as it might by the sale of its bonds, debentures or similar securities" (161 F. 2d at p. 595). Judge Chase went on to say: "The tax on debentures was not repealed and if debentures are issued and sold it is clear that they are none the less taxable because they are called promissory notes" (161 F. 2d at p. 595). To the same effect see: *Belden Mfg. Co.* v. *Jarecki,* 192 F. 2d 211 (7th Cir. 1951); *U. S.* v. *Ely & Walker Dry Goods Co.,* 201 F. 2d 584 (8th Cir. 1953). After examining all of the circumstances surrounding the transaction involved in the *General Motors* case the Court concluded that various factors (to which we shall refer a little later) "combined to put them [the notes] in a class apart from ordinary commercial promissory notes and into the category of debentures * * *" (161 F. 2d at p. 596). The Court's decision that the GMAC promissory notes were subject to stamp taxes went

on this ground, and not on the ground that only "short term" promissory notes were comprehended in the 1924 repeal of stamp taxes on promissory notes, nor on the ground that the purpose of the loan was in itself the controlling thing.

We find nothing in the earlier statutes which establishes either that the former stamp taxes on promissory notes or their repeal was limited to individual or short term promissory notes. Nor is the legislative history of these statutes illuminating on this score. The District Court in the present case in reaching the conclusion that the purpose of the 1924 repealer was "to relieve the poor *individual*" from stamp taxes referred to some of the debate on the floor of Congress in connection with the 1924 Revenue Act (112 F. Supp. at pp. 135-6).

An examination of the debates and committee reports preceding the enactment of the 1898 Statute, 31 Cong. Rec. 4263-4460, 4850-5749 (55th Cong., 2d Sess.), and those surrounding the succeeding statutes up to 1924 which imposed a tax upon notes, reveals nothing as to the scope of the promissory note taxing provisions.[3] Prior to the

[3] For the legislative history of the 1914 Act, see H. R. Reports Nos. 1163, 1193 and 1200 and S. Rept. No. 813 on H. R. 18891 (63d Cong., 2d Sess.); for the 1917 Statute, see H. R. Report No. 1366 and S. Report No. 1039 on H. R. 20573 (64th Cong., 2d Sess.), and H. R. Reports Nos. 45 and 172 and S. Reports Nos. 75 and 103 on H. R. 4280 (65th Cong., 1st Sess.); for the Revenue Act of 1918, see H. R. Reports Nos. 767 and 1037, and S. Report No. 617 on H. R. 12863 (65th Cong., 2d and 3d Sess.); and for the Revenue Act of 1921, see H. Reports Nos. 350 and 486 and S. Report No. 275 on H. R. 8245 (67th Cong., 1st Sess.).

1924 Act, the only discussion of the matter which we have found is contained in the Report of the House Ways and Means Committee on H. R. 12394 (which became the Act of March 2, 1901). In estimating the revenue loss contemplated as a result of repealing the note tax, Mr. Payne, Chairman of the Committee, predicated his estimates upon an opinion of the Comptroller of the Currency that notes taken by national banks ran, on an average, for ninety days. 34 Cong. Rec. 245 at 246-7 (56th Cong., 2d Sess.). But this statement can hardly be said to indicate a Congressional view that the notes previously taxed were only those which did not exceed this average. Moreover, a later statement in the same report that the Committee had "left on taxes in Schedule A which applied to transactions on stock exchanges in the large cities of the country, both in speculating in farm produce and also in buying and selling stocks and bonds on the market * * *" might be taken as an indication that Congress viewed bonds and debentures as essentially marketable investment instruments, as distinguished from commercial banking, promissory note transactions.

The debates relating to the 1924 repeal are also wholly inconclusive. While there are repeated references to the necessity for relieving "the old farmer who goes to the bank and renews his note every 90 days" from a recurring tax upon each renewal, and a reference to repealing the tax on "the misfortune of men," 65 Cong. Rec. 3277 (68th Cong., 1st Sess.), there is also a recognition that "a large part of the tax is paid by corporations who

borrow money by millions in the banks of the large cities." 65 Cong. Rec. 3279 (68th Cong., 1st Sess.). Similarly, emphasis in the debates on the 30-60-90 day transaction is counterbalanced by a recognition that some loans may extend over a period of as much as five years. 65 Cong. Rec. 3280 (68th Cong., 1st Sess.). And references to small loans are offset by other references which might be interpreted as an intention to remove the tax from all commercial bank transactions. See 65 Cong. Rec. 8199 (68th Cong., 1st Sess.). And the Committee reports on the 1924 bill, which would be more persuasive on the issue of legislative intent, hardly mention the matter at all.

The most that can be said from this meagre legislative history as to the 1924 repeal is that perhaps some members of Congress were especially concerned with exempting notes for small amounts on a 90-day term basis, but even such individual expressions to that effect must be read in the context of a debate which had a highly political backdrop.

By the same token, we think that neither these early statutes themselves nor their legislative history supports an argument that since Congress in 1924 repealed without limitation the pre-existing stamp taxes on "promissory notes" such notes under no circumstances can now be subject to stamp taxes. While we do not understand that such an argument is pressed by the appellant at bar, it was made (and rejected) in *General Motors Acceptance Corp.* v. *Higgins, supra,* at page 595, and in *Commercial Credit Co.* v. *Hofferbert,* 93 F. Supp. 562, 564 (D. Md. 1950).

Therefore, as we view the matter, the turning point in this case is whether the Niles-Bement notes, though termed "promissory notes," nonetheless have rather the attributes of corporate debentures so as to make them subject to stamp taxes under Sections 1800 and 1801 of the present Revenue Laws. Since neither Congress nor the Bureau of Internal Revenue has ever defined the term "debentures" under the stamp tax statutes, and the legislative history throws no light on the subject, we proceed to examine these promissory notes, and the transaction to which they relate, to determine whether they fit more the category of a debenture issue than a straightforward commercial loan, as those terms are commonly understood in the business world.

1. The notes here were typed on plain white paper and did not bear the corporate seal, in contrast to the *GMAC* notes which were printed on tinted paper with engraved borders, issued in serial form, and bore the corporate seal. These differences in appearance, while not of great weight, are at least of more significance in establishing the true genus of these instruments than the mere description "promissory notes" or "debentures." See: *U. S.* v. *Ely & Walker Dry Goods Co.* and *Belden Mfg. Co.* v. *Jarecki, supra.*

2. The restrictions placed on the activities of Niles-Bement by the Loan Agreement perhaps to some extent point away from this loan being the usual sort of commercial loan transaction. But we do not think that fact, standing alone, is controlling. In a loan of this magnitude such restric-

tions are not surprising; and we find nothing in the statutes or legislative history establishing that the size of the transaction is determinative of its tax consequences. See *Belden Mfg. Co.* v. *Jarecki, supra,* at page 214. For the same reason we discount appellant's emphasis on the fact that the *GMAC* loan was much larger than this one. GMAC was also much larger than Niles-Bement.

3. In this case the term of the loan was 7 years; the *GMAC* loan was for 5 years. But more significant is the fact that in the *GMAC* loan the maturity dates of the notes were bunched within the 6 months period at the close of the term, whereas here the notes matured at regular quarter-annual intervals, so that 36% of the loan was repayable during the first two years. This indicates that it was anticipated that the loan would be liquidated in the normal operation of the borrower's business, rather than, as in an "investment" context, from a more long-term realization on capital improvements.

4. In the *Niles-Bement* loan the borrower had the privilege of "prepayment," whereas the *GMAC* loan agreement referred to the same privilege as one of "redemption," a term more closely associated with traditional debenture financing. And the penalty for "redemption" under the *GMAC* loan was ¼% for each six months the term of the loan was shortened, whereas in this case the privilege of "prepayment" was "only in the inverse order of the maturity" of the notes, and the ¼% penalty was exacted only if such prepayment was followed by refinancing through another

lender during the term of the loan. Moreover, in *General Motors,* unlike the present case, the agreement required the borrower, at the lender's request, to break up the large notes into smaller ones, evidently for the purpose of marketability. Compare the presence of such a provision in *Gamble-Skogmo, Inc.* v. *Kelm,* 112 F. Supp. 872 (D. Minn. 1953), and in the *Commercial Credit* case, *supra* (which the taxpayers lost) with the absence of such a provision in the *Belden* and *Ely & Walker* cases *supra* (which the taxpayers won).

5. In *General Motors* the resolution initiating the borrowing authorized the officers to borrow about $30,000,000 from not more than "ten investors" and required that the lenders state that their "purchases" of the notes were for *investment* account, and not with a view of distribution to the public. Language of purchase and sale was consistently employed in the loan papers. The notes were sold at a negotiated price above par to reflect the interest rate adjustment, just as are traditional bonds and debentures. At least some of the notes were payable to bearer, and the lenders insisted on and received the right at their option to make all the notes fully marketable. Moreover, the lending institutions consisted principally of a group of five insurance companies, and one investment banking house, rather than commercial banks. In short, the *GMAC* notes had all the characteristics of an issue of marketable corporate securities, and the transaction itself all of the features of what is now known as a "private placement."

In holding that this combination of factors, and others already referred to, put the *GMAC* notes "in a class apart from ordinary commercial notes and into the category of debentures * * *," our Court stressed the investment nature of the transaction. To be sure, a bank as well as an insurance company in a sense intends to invest when it lends money, whether the transaction be called a loan, a private placement, or a public issue. But the classic feature demanded of an investment instrument is ready marketability, and that is what the *GMAC* notes had, and what the *Niles-Bement* notes did not have. And all the cases which have considered the matter appear to have read the *General Motors* case, as we do, as holding that only those instruments having the characteristics of an investment security fall within the terms of Section 1801. See, e. g., *United States* v. *Ely & Walker Dry Goods Co., supra,* at pages 588-89; *Belden Mfg. Co.* v. *Jarecki, supra,* at pages 213-14; *Stuyvesant Town Corp.* v. *United States,* 111 F. Supp. 243, 247-8 (Ct. Claims 1953).

In contrast to what appeared in the *General Motors* case, the *Niles-Bement* transaction was initiated along traditional loan lines by application to the Loan Department of the National City Bank, with which Niles-Bement had had ordinary commercial banking relations for twenty years; the interest rate was computed strictly on the face amount of the loan; no language of purchase and sale was used; there was no requirement of a statement of investment intention, nor any provision for break-

down of the notes to promote marketability; and none of the notes were payable to bearer.

We find here no such combination of factors as led the Court in the *General Motors* case to hold the promissory notes there in question taxable as debentures. We hold that the transaction in this case was a straightforward commercial loan, and that these promissory notes did not partake of the character of debentures.

Fundamentally the issue is a narrow one. Are these instruments "debentures"? We think they are not. Perhaps if we were drafting legislation on the subject we might think it desirable to require that stamps be affixed to documents such as these, or even to all promissory notes over a certain amount. But such matters of policy are for Congress to determine. If commercial bank loans such as we have before us here are to be brought within the ambit of this statute that is a matter for Congress, and not for the Courts, to decide. We do no more than construe the legislation as we find it.

Reversed.

CLARK, *Circuit Judge* (dissenting):

Judge Harlan's careful and extensive research into the legislative background of the revenue law here involved serves in my judgment to afford strong support for both the reasoning and the decision in *General Motors Acceptance Corp.* v. *Higgins*, 2 Cir. 161 F. 2d 593, certiorari denied 332 U.S. 810, now largely repudiated in actual result. The narrow distinction of the statute between promissory notes, which are not subject to the stamp tax,

and corporate debentures or certificates of indebtedness, which are, is not of our choosing and we have no authority to blot it out or even to soften it. So to do is unjustifiable judicial legislation in my view; and I cannot accept the indictment that the contrary interpretation by Judge Smith and myself is. For the approach of the *GMAC* decision and of Judge Smith below in a reasoned decision, D. C. Conn., 112 F. Supp. 132, which I should be glad to accept as my own, is but the appropriate and necessary execution of congressional intent to which we are by law obligated.

The *GMAC* decision was an outstanding milestone in the interpretation of the statute in several aspects. Perhaps most important was its stress on substance and debunking of form. And among the indicia as to substance which it notes, it does not give exclusive weight to the activity and intent of the *lender,* but rather emphasizes the attitude and need of the *borrower,* thus contrasting a corporation's "capital [obtained] for a substantial period of time from investors for general use in its business just as it might by the sale of its bonds, debentures or similar securities" with "the notes used customarily in day to day commercial transactions of a short time credit character." 161 F. 2d at page 595. While Judge Harlan's opinion does not expressly repudiate this holding, yet the present decision and its reasoning surely treads in the opposite direction. Its practical consequence, I suggest, is that bank loans are excepted from the tax, and the statute is amended to that extent—an obvious gain in simplicity, but obtained at the sacrifice of legis-

lative plan for relatively impartial distribution of tax burdens.

The conclusion I have just drawn from the opinion seems to me to follow from the distinctions it finds between this case and the *GMAC* case, framed in terms of distinctions between commercial loans and corporate debentures. As conceded, some of the features here present operate in favor of the conclusion reached below; these include the restrictions here placed on the borrower, the size of the borrowing, and its very substantial duration. In truth, I do not see anything to override their cumulative impact, any more than did Judge Smith. So the considerations found most significant—those numbered "3" and "5"—seem to me highly illustrative. They come from approaching the problem from the standpoint of the lender, not that of the borrower. Thus the regular intervals of maturity of the notes can mean to the maker only the same kind of amortization now usual in, say, a real estate mortgage. And the differences stressed in the handling of the loans as affects the lenders show convincingly that the real distinction thus isolated is between a "private placement" for such investors as insurance companies and an investment house, in the *GMAC* case, and a loan by a bank from its own loaning funds. If each suggested difference is actually examined, it becomes apparent that it is entirely for the lender's benefit and convenience in carrying on the business in the form to which it is accustomed. Consider the "classic feature" of "ready marketability," which it is said the present notes did not have. But this is only to say that of

course the National City Bank does not make a business of peddling its loans. And can there be doubt that investors would gladly invest in loans made and negotiated to them by that Bank if they were given opportunity?

The point may be underlined by considering the application of this case as a precedent to future borrowings. A borrower considering how to avoid the additional burden of the stamp tax would see that not his needs or assumed obligations, but rather the source of supply of the funds, would be decisive. Since he can thus easily satisfy his needs in the one fashion as the other, he naturally will go to the lender who has the advantage of also giving him freedom from the burden of the stamp tax. And that is the kind of one-sided advantage to bank loans now read into the act which does seem to me to be deplored.

A recent analysis of this problem, "Stamp Tax on Promissory Notes Representing Term Loans and Private Placements," 54 Col. L. Rev. 428-431 (March, 1954), supporting the *GMAC* decision and the holding below, seems to me to call attention to criteria which have been overlooked in my brothers' opinion. The writer says (footnotes omitted):

> "As of 1924 the 'promissory note' in corporate borrowing evidenced short term commercial loans arising in the ordinary course of business—rather than capital loans—and it is probably from the former that Congress intended to remove the tax. The confusion in the recent cases is apparently due to two signifi-

cant post-1924 developments in corporate financing practice: the bank 'term loan' and the private placement with institutional investors. All of the *GMAC* line of cases involved notes representing either term loans or private placements and the courts, usually without recognition that they are dealing with changed methods of corporate finance, have attempted to fit them within the traditional security-promissory note dichotomy." 54 Col. L. Rev. at 429, 430.

Then, after consideration of "private placement" as "a broad term describing all directly negotiated financing between a corporation and an institutional investor, usually an insurance company," and of "term loans" by a bank, which occupy "an anomalous position," being "neither investment nor loan according to traditional banking practice," the author continues:

"With respect to these new forms of corporate finance, it is apparent that the lender's motive in treating the transaction as loan or investment is not a helpful guide in determining taxability. Under this view the borrower is subject to the tax when the lender 'intends to invest.' But since privately placed loans are generally treated as investments and term loans do not fall within either category, if this distinction is pursued it is conceivable that a term loan note negotiated with the loan department of a bank would be non-taxable through an identical note privately placed with an insur-

ance company would be taxed. Similarly, distinctions based on the instrument's marketability do not seem substantial in view of the common provision for converting the note into marketable instruments.

"In light of the meaning of 'promissory note' in 1924 and the subsequent growth of private placement and term loans, the view of the courts following the *GMAC* case seems the wiser one. The opposing decisions, emphasizing the loan-investment distinction and marketability, run counter to the apparent Congressional intent to leave taxable loans of substantial duration to be used by the borrower for capital purposes. By including within the term 'promissory note' of the 1924 amendment instruments representing the newer methods of corporate finance, these decisions fail to construe these words in light of their meaning at the time of enactment." 54 Col. L. Rev. at 431.

Following this appropriate and clear-cut analysis, I would affirm.

☆ U. S. GOVERNMENT PRINTING OFFICE: 1968 [illegible]